





Cover

The background of the flame highlights an area of the Alberta foothills where Union is heavily involved in a search for major natural gas reserves. The photographs appearing inside the cover are typical scenes of the area.

Map reproduced from MCR 81 by permission of the Surveys and Mapping Branch, Department of Energy, Mines and Resources, Ottawa.

The Company

The Company was incorporated under the laws of Canada in 1921 as a wholly owned subsidiary of Union Oil Company of California. At that time its primary business was petroleum marketing and distribution. In 1945 the Company sold its marketing facilities. In the late 1940's Union Oil Company of California became actively engaged in Canada in petroleum exploration and development. In 1961 Union Oil Company of Canada Limited became a public company and Union Oil Company of California conveyed its oil and gas properties in Canada to the Company in exchange for approximately 83% of the issued stock. The public purchased the balance of the shares offered.

Union of Canada expanded its operations by acquiring Williamson Oil and Gas Ltd. in 1962 and E. H. Vallat Ltd. in 1963. These companies were merged into Union Oil Holdings Limited which remains as the Company's only subsidiary.

In 1965 the Company further expanded with the acquisition of the Canadian petroleum properties of the Pure Oil Company from Union Oil Company of

California in exchange for additional shares which brought Union Oil Company of California's interest in the Company to its present level of 86.7%.

The Company constructed a refinery in British Columbia in 1966 and commenced marketing petroleum products in western Canada. During 1976 it was decided that, rather than make the additional substantial capital investment necessary to remain competitive, the Company should dispose of the assets of the refining and marketing division and increase natural resource exploration and development.

In 1975 the Company formed a Mineral Department and commenced the exploration for coal, uranium and base metals and now holds a 90% interest in a promising thermal coal property near Hinton, Alberta.

Union's objective is to build a stronger and more profitable company by expanding natural resource exploration and development, with emphasis on the energy fuels; petroleum, coal and uranium in western Canada.

Highlights

	1977	1976	Increase (Decrease) Percent
Financial			
Total revenues	\$ 82,398,000	\$104,595,000	(21)
Cash flow from operations	42,785,000	34,704,000	23
per share	2.97	2.41	
Earnings from operations	20,489,000	15,486,000	32
per share	1.42	1.08	
Dividends	3,744,000	3,024,000	24
per share	0.26	0.21	
Capital and exploration expenditures	44,101,000	27,030,000	63
Working capital at year end	26,631,000	21,983,000	21
Average shareholders' equity	\$110,300,000	\$128,735,000	(14)
Return from operations on shareholders' equity (percent)	18.6	12.0	55
Operating			
Gross daily production			
Crude oil and natural gas liquids (bbls) .	27,974	27,399	2
Natural gas (mcf)	69,016	68,461	1
Sulphur (long tons)	198	228	(13)
Gross proven reserves at year end			
Crude oil and natural gas liquids (thousands of barrels)	117,578	126,727	(7)
Natural gas (mmcf)	632,582	595,692	6
Sulphur (thousands of long tons)	885	1,000	(12)
Land holdings at year end (thousands of net acres)			
Petroleum	6,069	6,494	(7)
Mineral	255	308	(17)

To Our Shareholders



The year 1977 was one of the most successful and rewarding in your Company's history. Substantial progress was made toward accomplishing our corporate objectives of profit improvement and expansion of natural resource exploration and development.

In our 1976 report we forecast continued improvement in earnings, cash flow, return on shareholders' equity and an increase in capital and exploration expenditures. Results for 1977 were:

- Earnings from operations up 32% to \$20.5 million
- Cash flow from operations increased 23% to \$42.8 million
- Return from operations on shareholders' equity rose from 12% to 18.6%
- Capital and exploration expenditures increased 63% to \$44.1 million.

The improved financial results were largely due to price increases. New crude oil and natural gas production was sufficient to balance decline in older properties and production lost to market pro-rationing in Alberta.

The 1977 petroleum exploration and development program was the largest and one of the most successful in our history. Expenditures increased 56% to a record \$37.7 million. About 80% of the total was spent in Alberta with major emphasis on foothills natural gas prospects. The foothills program resulted in a significant natural gas discovery and acquisition of additional land which will provide a strong base for 1978 drilling. Expenditures for land increased 125% to \$14.0 million and, in addition to the foothills, included acquisitions in high potential areas such as West Pembina in central Alberta and Elmworth-Wapiti in northern Alberta and British Columbia. Proven and potential reserves indicated by exploration and development drilling should more than replace the total equivalent barrels of oil and natural gas produced in 1977.

Union's crude oil and natural gas liquids production increased 2% in 1977 to 27,974 barrels per day. A 39% increase in Saskatchewan production was sufficient to offset declines in Alberta and British Columbia. During 1977 Union's Alberta production of light and medium conventional crude averaged 12,800 barrels per day, about 80% of capacity. Alberta production has been pro-rated, primarily as a result of reduced exports to the United States. Further pro-rationing will occur in 1978 as new production from

the Syncrude plant and West Pembina will capture a significant share of the market for Alberta crude. Faced with increasing supply and a relatively static market we do not expect Union's shut-in Alberta capacity to be marketed in 1978.

Your Company's natural gas sales remained essentially unchanged at 69.0 million cubic feet per day in 1977. Production from new sources offset decline in older fields and the reduction in take by major purchasers in Alberta. The only foreseeable solution to the rapidly growing natural gas surplus in Alberta is additional sales to the United States. About 25% of Union's natural gas reserves are not contracted for sale. We can afford a reasonable lead time from discovery to sale but will eventually require increased sales if we are to maintain an aggressive exploration and development effort. Consequently, we will increase our effort to find natural gas in British Columbia where there is an available market.

We believe that a portion of cash flow should be directed to long-term investments in our future. Therefore, we plan to continue and expand our non-conventional heavy oil research project in northern Alberta. We have obtained good results from steam stimulation and plan to investigate other recovery techniques.

To maintain growth and diversification we are continuing to pursue new ventures in mineral exploration and development. We have been very encouraged by the progress of our various studies relating to development and marketing of a thermal coal reserve near Hinton, Alberta. We believe the property will support the mining of 4.5 million short tons per year of raw coal from a potential reserve of 200 million short tons. An operation of this scale would result in sales of 3.0 million short tons per year of clean coal.

The rapid increase in the complexity, scale and cost of our operations must be dealt with by a flexible and efficient organization, additional staff and a constant upgrading of skills. In recognition of these needs the basic corporate organization has been restructured during the past two years, and highest priority given to recruiting and professional development.

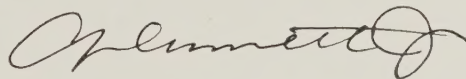
The Company is fortunate to have a dedicated and experienced group of employees. The success achieved in 1977 would not have been possible without their enthusiasm and hard work. On your behalf we congratulate them on a job well done.

The outlook for Union in 1978 is good. Financial results will continue to improve as a result of rising

prices and increased natural gas sales. Although governments, through royalty and taxation, retain over 75% of the benefits accruing from price increases the portion retained by industry has provided sufficient incentive to increase exploration to record levels in Alberta and British Columbia. We are optimistic about our exploration plans for western Canada where continued emphasis will be placed on finding significant new reserves in the foothills and deeper parts of the sedimentary basin. Capital and exploration expenditures will exceed the record level attained in 1977.

Late in the year, Mr. J. C. Browning, Vice President, Corporate Affairs, announced his intention to take early retirement effective January, 1978. Mr. Browning's experience and sound advice will be missed. On December 2, 1977, Mr. D. B. Jarrett, formerly Comptroller and Assistant Secretary, was appointed Vice President, Administration and Mr. J. J. Bohnet, formerly Manager of Accounting, was appointed Comptroller and Assistant Secretary.

ON BEHALF OF THE BOARD



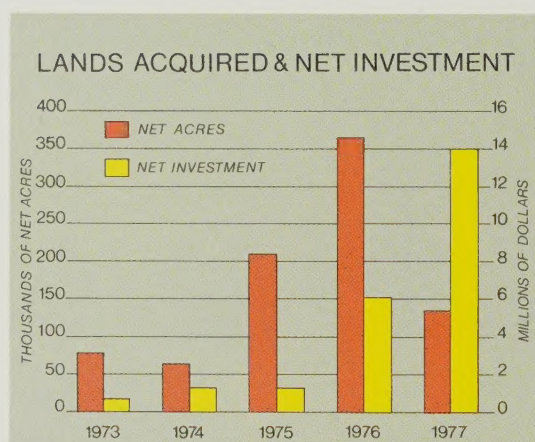
C. W. DUMETT, JR.
President

February 24, 1978.

Petroleum Exploration and Development



E. D. B. Laudeman



Exploration and development expenditures in 1977 were the largest in the Company's history, reaching \$37.7 million, a 56% increase over 1976. As planned, emphasis was placed on acquiring highly prospective lands for drilling in 1978 and 1979. Land expenditures totalled \$14.0 million, a 125% increase over the \$6.2 million spent in 1976. The bar graph sets out the number of exploratory net acres acquired by the Company in Canada during the past five years and their cost.

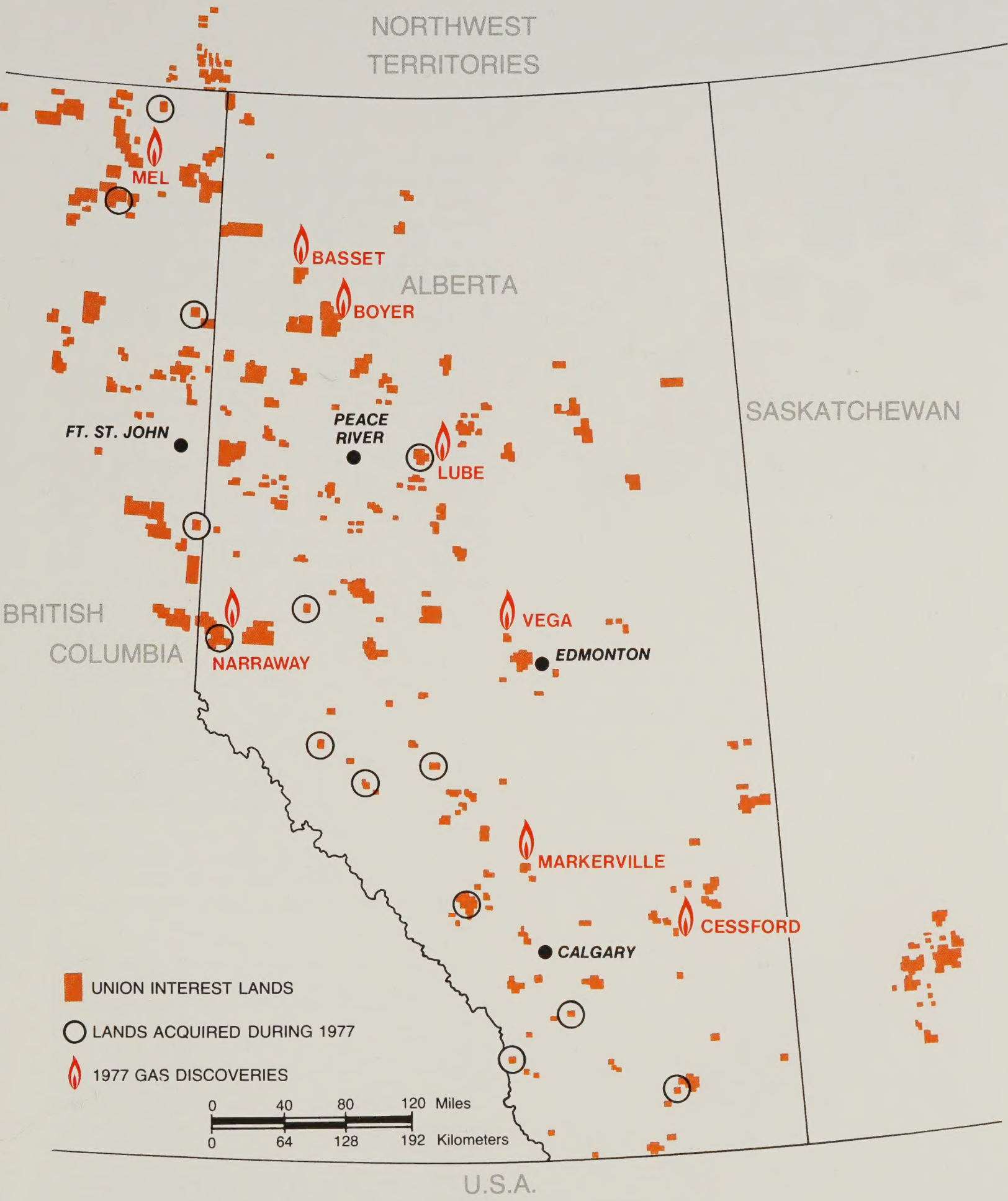
Union participated in a total of 92 exploratory and development wells of which 68 were completed for oil and gas production, two as service wells and 22 abandoned. The proven and potential reserves indicated by this program should more than replace total equivalent barrels of oil and natural gas produced during 1977, although several years of development drilling will be required to convert the potential reserves to proven.

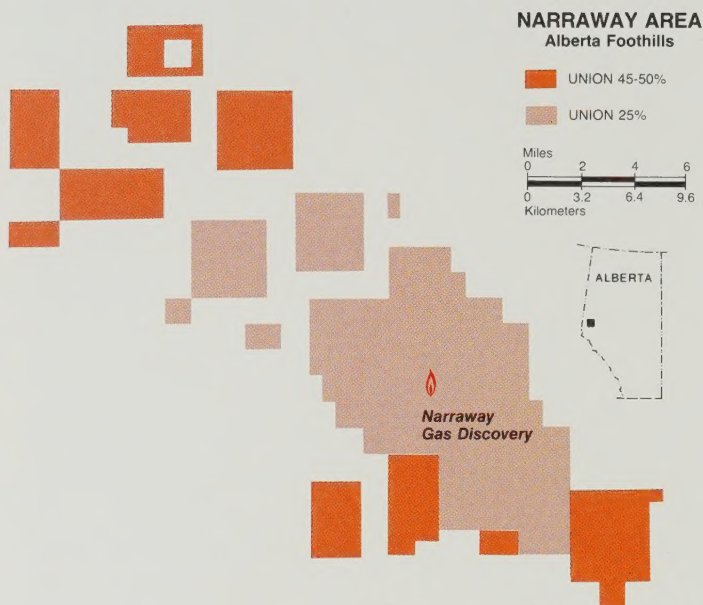
The majority of exploration spending was directed to Alberta where the Company continued its effort to develop natural gas prospects in the foothills. The foothills program resulted in a significant natural gas discovery and acquisition of lands which will provide a strong base for additional drilling in 1978. Also in Alberta Union acquired varying interests in 2,560 acres at West Pembina which are considered highly prospective for Devonian oil.

Activity in British Columbia was highlighted by the acquisition of additional acreage near the Alberta border in the rapidly developing Elmworth-Wapiti natural gas play. Union now holds interests in 212,500 acres in this area and will participate in the drilling of at least five exploratory wells in 1978. Further north a substantial effort was directed to the Slave Point Devonian shale basin in the search for pinnacle reefs. This program resulted in one natural gas discovery and the acquisition of additional land. Union now holds interests in 240,000 acres in this area.

As a result of the many exploration opportunities the Company has developed within Alberta and British Columbia, only a limited amount of manpower and financial resources were directed to other parts of Canada and international areas in 1977.

Union participated as a 25% partner in the first discovery of natural gas offshore in the Bay of Bengal, Peoples Republic of Bangladesh. The well produced gas at rates of up to 18 million cubic feet per day. However, the economic importance of the discovery is uncertain.





Alberta

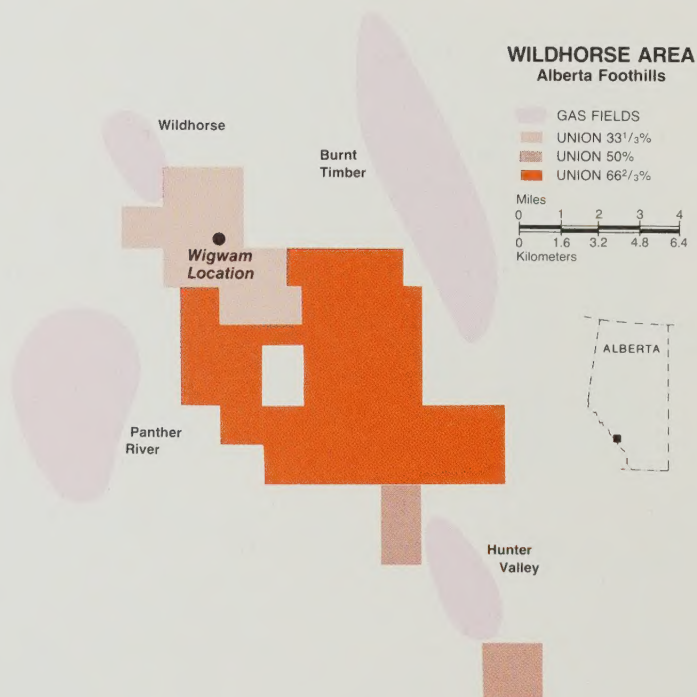
In 1977 the Company's exploration program was directed primarily to Alberta where emphasis was placed on obtaining additional land to further increase our base for natural gas exploration in the foothills. The foothills program was a continuation of 1976 activity which included the formation of several joint venture groups. The adjoining maps illustrate some of the major land blocks which the Company wishes to highlight.

The foothills program included participation in four wells, the purchase of 52,000 gross (23,181 net) acres and the acquisition of 946 miles of seismic data. One well resulted in a significant natural gas discovery, one was abandoned and two were drilling at year end. The discovery well, C.S. et al Narraway 5-3-63-11-W6M, (Union 25%), was completed in September. Shortly after completion Union and partners acquired a 23,040 acre Crown license surrounding the well for a total bid of \$4.2 million. Other land blocks were purchased in the Wildhorse area which lies about 60 miles northwest of Calgary near the Burnt Timber natural gas field. Union (66²/₃%) and a partner acquired a 22,720 acre Crown license in May for a total bid of \$6.1 million. In August Union (50%) and the same partner purchased an additional 2,720 acres in this area for \$3.0 million. A well, Wigwam 2-12-31-10-W5M, to test this prospect will commence drilling in the first quarter of 1978. Union's share of land bonuses amounted to about 10% of total industry expenditures for Crown land in the Alberta foothills during 1977. Additional lands were acquired by farm-in from other companies.

In other parts of Alberta, exploration and development drilling established new natural gas reserves at Bassett, Boyer, Cessford, Lube, Markerville and Vega.

In total the Company acquired 134,552 gross (92,249 net) acres in Alberta. Acquisitions outside the foothills were highlighted by the purchase of interests varying from 22.5% to 38% in 2,560 acres at West Pembina at a cost of \$3.5 million. In addition, negotiations were in progress to acquire more land in this area. West Pembina, an older oil producing region, is now experiencing exploration for deep Devonian oil, and discoveries to date indicate a new producing trend of major significance.

Seismic operations in Alberta resulted in the total acquisition of 1,879 miles of data for specific prospects and regional evaluations.





British Columbia

The main effort of exploration and development was in continued evaluation of lands and projects for drilling in the Slave Point Devonian shale basin and the Elmworth-Wapiti area. A significant amount of seismic was conducted on Union lands to develop drillable prospects. Further seismic was done in other areas in preparation for land acquisition. In total 752 miles of seismic data was acquired. Lands totalling 85,539 gross (39,582 net) acres were purchased in four prospect areas.

Three exploratory wells were drilled in the Province; one was completed as a gas well and two were abandoned. The discovery well, CDC et al Mel c-57-J, 94-P-4 (Union 40%), was drilled on a Slave Point pinnacle reef anomaly. A service rig is scheduled to move in and test the well early in 1978. Development drilling in the Province totalled six wells; three of which were completed as gas wells, one as an oil well and two were abandoned.

By year end Union had several major exploration programs underway, two of which, the British Columbia foothills and the Slave Point pinnacle reef area,

will result in large seismic expenditures and additional land acquisition in preparation for increased drilling activity. Union has expanded its activity in the Elmworth-Wapiti area where it holds interests ranging from 37.5% to 100% in 212,500 acres outlined on the adjoining map. During 1977 more than 30 widely spaced natural gas wells were completed just across the border in Alberta. Favourable markets for natural gas and optimism that this trend will continue into British Columbia are expected to lead to a high level of industry activity in 1978. At year end, Kelly b-28-I, 93-P-1 (Union 50%) was drilling to test this prospect and at least five additional exploratory wells will be drilled on these lands in 1978.

Union's exploration and development expenditures in British Columbia should increase significantly in 1978.

Petroleum Land Holdings at December 31, 1977 (acres)

Region	Permit/Reservation/License		Leasehold		Total	
	Gross	Net	Gross	Net	Gross	Net
Alberta	877,127	791,901	1,588,262	961,290	2,465,389	1,753,191
British Columbia	959,790	473,430	707,551	349,698	1,667,341	823,128
Manitoba	—	—	1,960	890	1,960	890
Saskatchewan	—	—	160,224	56,091	160,224	56,091
Federal Lands	4,525,319	2,793,602	277,442	144,658	4,802,761	2,938,260
TOTAL CANADA	6,362,236	4,058,933	2,735,439	1,512,627	9,097,675	5,571,560
Bangladesh	1,989,120	497,280	—	—	1,989,120	497,280
TOTAL	8,351,356	4,556,213	2,735,439	1,512,627	11,086,795	6,068,840

Saskatchewan

With the improving market for medium gravity crude oil Union and partners drilled a total of 27 development wells in the Province. Of these wells, 23 were completed for oil production, one as a gas well, two as service wells and one was abandoned. The Company has also initiated exploration programs directed at finding new reserves of oil and gas. A geophysical program was completed in late 1977 and studies are underway which may lead to increased interest in Saskatchewan exploration.

Drilling Operations				
	1977		1976	
	Gross	Net	Gross	Net
EXPLORATORY WELLS				
Oil	4	2.5	—	—
Gas	20	14.3	18	10.2
Dry	18	10.5	18	11.4
TOTAL	42	27.3	36	21.6
DEVELOPMENT WELLS				
Oil	28	7.5	9	2.4
Gas	16	9.4	18	12.4
Service	2	.6	3	.6
Dry	4	1.8	7	3.4
TOTAL	50	19.3	37	18.8

Frontier Canada

The Company's work in 1977 was limited to maintenance of its 2.9 million net acres in the Northwest and Yukon Territories, Arctic Islands, Beaufort Sea and westcoast offshore. The announcement of a natural gas pipeline to be built along the Alcan highway, rather than through the Mackenzie Valley in Canada, will further delay production from the Mackenzie Delta and Beaufort Sea. Accordingly, the Company's activity on lands in frontier areas of Canada will be limited until economic and operational factors improve.

Discoveries of oil and natural gas in the Beaufort Sea have established this area as having significant petroleum potential. Union plans to maintain its 50% position in 556,000 gross acres in this area by meeting all regulatory requirements. The work commitment for 1978 will be met by a sizeable offshore seismic program.

International

Union continued to review exploration prospects outside the continental limits of North America. However, the Company expects that the many exploration op-

portunities which are available in Canada will fully utilize its financial and personnel resources for some years.

Union's 25% participation in an exploratory offshore well in the Bay of Bengal, Peoples Republic of Bangladesh, resulted in a gas discovery. The well, drilled on a 2.0 million acre block, produced natural gas at rates of up to 18.0 million cubic feet per day. Further drilling will be deferred until a market is developed.

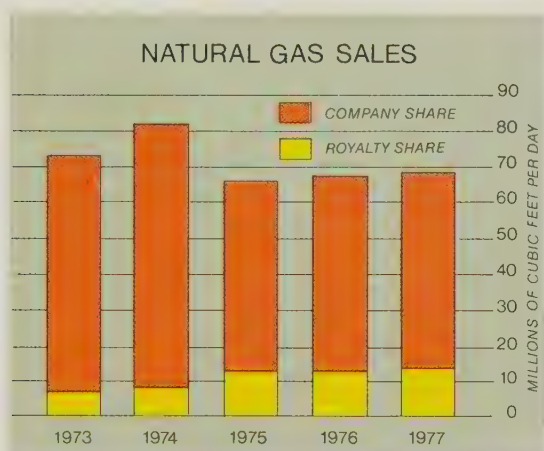
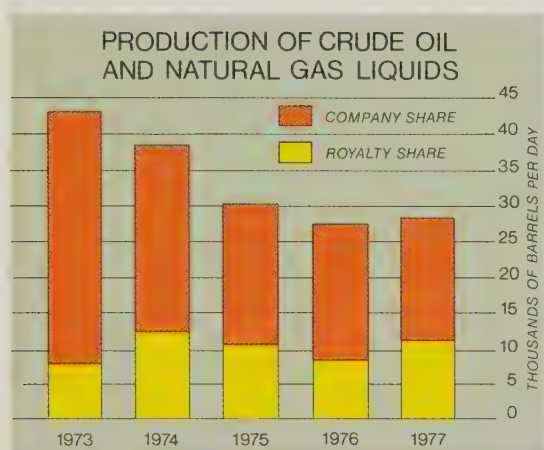
Outlook for 1978

Planned expenditures for petroleum exploration and development will increase in 1978. Areas of concentration will include the Alberta and British Columbia foothills, the Elmworth-Wapiti area and West Pembina. Alberta will continue as the Company's major area of investment, but expenditures should also increase in British Columbia and Saskatchewan.

Petroleum Production



E. J. Connor



Production revenue increased 27% to \$80.2 million in 1977, primarily as a result of price increases. Only modest gains were achieved in gross production of crude oil and natural gas liquids and natural gas.

Gross proven barrel equivalent reserves declined 2% to 209.4 million barrels as proven additions from new drilling and performance adjustments did not completely replace 1977 production.

The Company continued its non-conventional heavy oil, or bitumen, research program at Chipewyan in northern Alberta. Research into steam recovery techniques was conducted at two sites and plans are under development to expand this operation.

Two problems facing the Company early in 1977 became more serious as the year progressed. First, the natural gas surplus in Alberta continued to grow and little progress was made to establish new markets. At year end, about 25% of Union's natural gas reserves are not contracted for sale. Second, the high level of industry activity has created a very serious shortage of drilling rigs. This problem will adversely affect the Company's plans to increase drilling operations.

Crude Oil and Natural Gas Liquids

Gross crude oil and natural gas liquids production increased 2% in 1977, to 27,974 barrels per day. A 39% increase in Saskatchewan production, due to improved demand for medium gravity crude, was sufficient to offset production decline in older fields in Alberta and British Columbia and market pro-rating in Alberta.

Net revenue from liquids production rose 19% to \$58.5 million as a result of price increases. The average per barrel selling price for crude oil and natural gas liquids increased to \$9.73 as compared to \$7.45 in 1976, and further increases are expected in 1978.

Natural Gas

Gross natural gas sales averaged 69.0 million cubic feet per day as compared to 68.5 million cubic feet per day in 1976. Although production from new sources averaged about 11.0 million cubic feet per day, approximately 5.3 million cubic feet per day were lost because of decline in older fields and 5.2 million cubic feet per day by reduction in take by major purchasers in Alberta. Reduced purchases in Alberta were caused by the surplus natural gas reserves which have been developed over the past three years. This surplus is growing and unless new markets are found natural gas exploration will eventually be curtailed.

Crude Oil and Natural Gas Liquids Production

	Average Gross Barrels/Day		Average Net Barrels/Day	
	1977	1976	1977	1976
ALBERTA				
Kaybob South	7,718	8,381	4,753	5,316
Red Earth	3,052	2,944	1,924	1,909
Sturgeon Lake South	2,421	2,084	1,376	1,236
Virginia Hills	2,259	2,602	1,265	1,503
Other	1,800	2,012	1,277	1,511
	<u>17,250</u>	<u>18,023</u>	<u>10,595</u>	<u>11,475</u>
BRITISH COLUMBIA				
Milligan	866	1,310	473	620
Aitken	858	1,008	412	450
Peejay	376	459	224	241
Other	572	715	323	371
	<u>2,672</u>	<u>3,492</u>	<u>1,432</u>	<u>1,682</u>
SASKATCHEWAN				
Cantuar	1,122	675	596	576
Battrum	951	565	629	477
Fosterton	595	400	293	314
Instow	433	266	213	212
Steelman	421	472	201	373
Delta	392	246	213	213
Other	3,913	3,027	2,106	2,479
	<u>7,827</u>	<u>5,651</u>	<u>4,251</u>	<u>4,644</u>
MANITOBA	225	233	193	200
TOTAL	<u>27,974</u>	<u>27,399</u>	<u>16,471</u>	<u>18,001</u>

Natural Gas Sales

	Average Gross Mcf/Day		Average Net Mcf/Day	
	1977	1976	1977	1976
ALBERTA				
Kaybob South	14,326	16,794	8,165	9,836
Dunvegan	5,363	7,343	2,919	4,312
Youngstown	3,842	38	2,606	26
Crossfield	2,734	3,041	2,324	2,585
Other	11,848	11,520	8,848	8,708
	<u>38,113</u>	<u>38,736</u>	<u>24,862</u>	<u>25,467</u>
BRITISH COLUMBIA				
Clarke Lake	14,023	16,372	13,948	16,265
Aitken	4,586	—	4,535	—
Kotcho	3,269	1,279	3,269	1,279
Willow	2,436	3,107	2,407	3,067
Silverberry	1,885	3,829	1,885	3,829
Other	3,535	2,932	3,463	2,871
	<u>29,734</u>	<u>27,519</u>	<u>29,507</u>	<u>27,311</u>
SASKATCHEWAN	<u>1,169</u>	<u>2,206</u>	<u>1,043</u>	<u>2,074</u>
TOTAL	<u>69,016</u>	<u>68,461</u>	<u>55,412</u>	<u>54,852</u>

Net revenue from natural gas increased 54% to \$20.8 million due mainly to price increases. The average selling price increased to \$1.03 from \$0.68 in 1976 and should increase further in 1978.

Sulphur

Gross sulphur sales rose 7% to 231 long tons per day. Net revenue increased 59% to \$874,000 as the average selling price increased to \$12.43 from \$8.40 per long ton.

Average Selling Price Per Net Unit

	1977	1976	1975	1974
Crude Oil & Natural				
Gas Liquids (\$/bbl)	9.73	7.45	6.47	4.94
Natural Gas (\$/mcf)	1.03	0.68	0.54	0.26
Sulphur (\$/long ton)	12.43	8.40	10.72	8.42

Reserves

The Company's gross proven reserves at year end, as calculated by staff reservoir engineers, are summarized in the accompanying table. These figures include both developed and undeveloped reserves. Developed reserves are the quantities that can be recovered through existing facilities. Undeveloped reserves are the volumes estimated to be recoverable from wells to be drilled on proven acreage, from re-completion of existing wells or from the installation of new facilities. Potential or probable reserves, such as natural gas offshore Bangladesh or bitumen in northern Alberta, are not included.

Crude oil and natural gas liquids reserves declined by 9.1 million barrels to 117.6 million barrels as proven additions and engineering adjustments did not match production. Natural gas reserves increased 6% to 632.6 billion cubic feet. The overall result was a 2% decline in total barrel equivalents to 209.4 million barrels.

Gross proven reserves reflect the Company's ownership interest before deducting royalties. Reporting on a gross basis provides more reliable year end reserve data and facilitates year to year comparison of performance. Net reserves projections are less reliable as a result of the frequent changes in basic royalty rates and supplementary royalties which may vary with price and production rates. An approximation of net reserves may be obtained by using ratios of net to gross 1977 production from totals provided in the tables.

Operations

Expenditures for production facilities were \$1.7 million in 1977 and were directed to equipment for new wells and construction of a small gas plant at Tangent, Alberta.

Compression facilities at the Kaybob South gas plant, in which Union holds a 35.5% interest, were severely damaged by fire in December. The total damage is estimated at \$6.0 million and repairs will likely not be complete until July, 1978. Both repairs and loss of revenue are largely covered by insurance.

An additional \$2.3 million was invested in non-conventional heavy oil research. Non-conventional heavy oil, perhaps better known as bitumen, is defined as a naturally occurring viscous mixture of heavy hydrocarbons which is not recoverable by normal production practices without application of external heat. This research program, focused on the Grosmont carbonate formation, is located on a 100% Union holding of 155,000 acres at Chipewyan in northern Alberta. The Company believes that, as the demand for energy increases, this resource will grow in value and Union looks at the research program as a long-term investment in its future. Bitumen in place on this property is estimated at about 20 billion barrels. During 1977, research into steam recovery was conducted at two pilot sites with encouraging results. Operations will continue utilizing different recovery techniques at one site in 1978 and plans are being developed to expand operations in future years.

Negotiations are in progress to pool adjoining acreage with another company and share the high costs of large scale pilot operations. To the best of Union's knowledge, the Chipewyan project is the only research program in Canada aimed at recovering bitumen from a carbonate reservoir.

Outlook for 1978

It is anticipated that 1978 production of crude oil and natural gas liquids could be down by as much as 5% because of the Kaybob fire and more severe pro-rating in Alberta. Natural gas production should be up slightly above the 1977 level. However, the full effect of 1977 price increases and additional increases expected in 1978 should result in a substantial improvement in production revenue.

Expenditures for production facilities and heavy oil operations will increase in 1978.

Gross Proven Reserves

	Crude Oil & Natural Gas Liquids (Thousands of Barrels)	Natural Gas (Millions of Cubic Feet)	Sulphur (Thousands of Long Tons)	Total Barrel Equivalents* (Thousands of Barrels)
Reserves at December 31, 1976	126,727	595,692	1,000	213,492
Additions	802	58,034	—	9,093
Production	(10,211)	(25,191)	(72)	(13,930)
Engineering adjustments	260	4,047	(43)	767
Reserves at December 31, 1977	117,578	632,582	885	209,422
Total barrel equivalents* (thousands of bbls.)	117,578	90,369	1,475	209,422
By Region at December 31, 1977				
Alberta	81,717	405,248	885	141,085
British Columbia	3,905	192,535	—	31,410
Manitoba	381	—	—	381
Saskatchewan	31,575	27,853	—	35,554
Northwest Territories	—	6,946	—	992

*The ratios for converting natural gas and sulphur to equivalent barrels of crude oil and natural gas liquids are related to average prices received during the year: 1 barrel = 7 MCF of natural gas = 0.6 long tons of sulphur.

Mineral Exploration and Development



D. B. Leitch

In 1977 mineral exploration and development expenditures increased 174% to \$2.0 million. Exploration emphasis was placed on coal and uranium. Development of the Obed/Marsh thermal coal property continued and a detailed feasibility study was completed at year end.

Exploration

The continuing coal exploration program in Alberta resulted in the acquisition of 35,000 acres of coal leases. Evaluation drilling on the new lands will be initiated in 1978 and will continue on other previously identified prospects in Alberta. In addition, Union plans to explore for coal deposits in other parts of Canada.

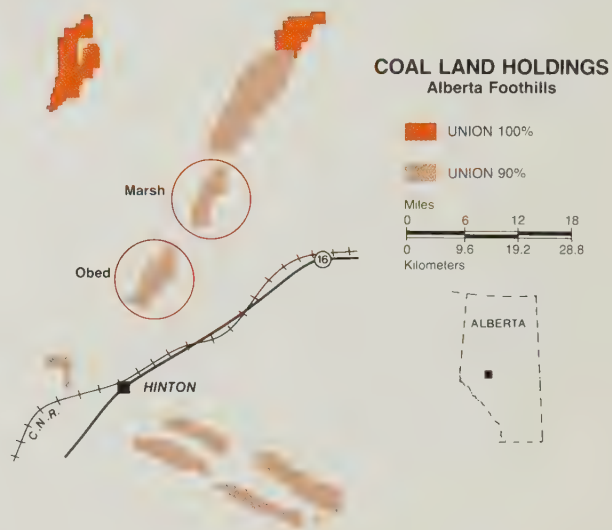
The Company participated in seven exploration programs for uranium which resulted in the staking of a number of claim blocks in the provinces of British Columbia, Manitoba and Ontario. Diamond drilling to evaluate the more attractive lands will be conducted in 1978.

The results from five exploration programs for base metals led to the staking of a large claim block in the Yukon Territory and two smaller blocks in British Columbia. Evaluation programs on these holdings are scheduled for 1978.

Development

Development activity was confined to the Obed/Marsh thermal coal leases located 15 miles north-east of Hinton, Alberta as illustrated on the adjoining map. During the year Union's interest in these leases was increased from 80% to 90%.

Assessment drilling and bulk sampling established the necessary reserve and quality parameters to proceed with a production feasibility study. The study was complete at year end and confirms that the Obed/Marsh property has potential for commercial production by surface mining techniques. The coal has a low sulphur content and a heat value in excess of 10,000 Btu/lb. Union believes the property will support the mining of 4.5 million short tons of raw coal per year from potential reserves in excess of 200 million short tons. This type of mining operation should result in annual sales of 3.0 million short tons of clean coal.



Discussions with prospective purchasers in the United States, Japan and Korea have been encouraging. However, to be competitive with alternate energy sources and coal exports from other countries, western Canadian coal must overcome several disadvantages. These problems include long distance railway charges, high labour and equipment costs, stringent environmental controls and high rates of royalty and taxation. Despite these problems Union believes that Obed/Marsh thermal coal will eventually prove competitive in world markets and the Company is proceeding toward a production decision.

Outlook for 1978

Total expenditures will increase over the level established in 1977 and exploration programs will continue to emphasize coal and uranium.

Administration

During the year the Company added 31 employees to its staff and at year end had 303 permanent employees, 269 of whom were located at the Company's head office in Calgary. The balance of the staff are engaged in field operations at Fort St. John, British Columbia; Slave Lake, Alberta and Oxbow, Saskatchewan.

Due to the Company's growth, and the resulting need for additional staff, Union has intensified its recruiting and professional development programs. All employees are encouraged to enroll in job-related educational courses. In 1977, 22 employees utilized the Company's Educational Assistance Program and a further 97 employees participated in a wide variety of technical training seminars.

The Company provided summer employment to 35 university and technical school students. This program assists the students financially and provides practical job experience. In addition, both the student and the Company can better decide if there is a mutual desire for continued employment following graduation.

The Company is fortunate to have many long-term employees. During the year 24 of these received service awards, seven of which were for service of ten years or greater.

The Company regularly reviews all employee benefit plans to ensure the provisions cover the present and

future needs of its employees. During 1977 significant changes were made to the Retirement Plan. These were a revised annuity formula, new vesting provisions and a survivor death benefit. In addition, benefits under the Non-Contributory Group Life Insurance Plan were increased. The total cost of payroll and employee benefits in 1977 amounted to \$7.1 million.

In recognition of its role in the business community the Company supports a large number of health and welfare agencies, cultural organizations and educational institutions. Financial assistance totalling \$158,000 was granted during the year.

Union actively participates in a number of industry associations and foundations, including the Canadian Petroleum Association and the Independent Petroleum Association of Canada. These associations provide alternate and collective means of making representations to the various levels of government and the general public.

Outlook for 1978

Union's plans for 1978 indicate increased activity in all areas of the Company. To meet these growth objectives, emphasis will continue to be placed on manpower planning and development.



Left to right: J. L. Maclagan, R. G. Byers, D. B. Jarrett and J. J. Bohnet

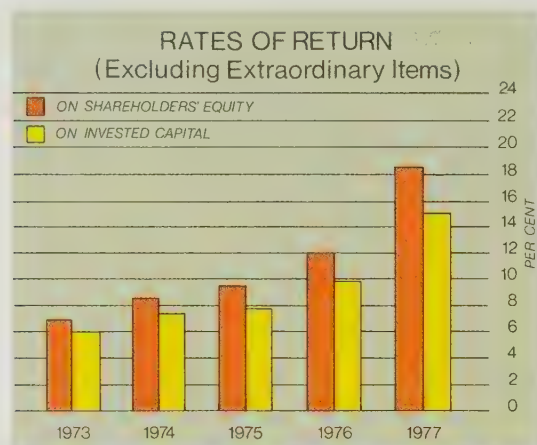
Financial Summary and Analysis

The financial results presented in this report for the year 1977 indicate significant gains. Net earnings, cash flow and return from operations reached new highs and further improvement is forecast for 1978.

Earnings and Cash Flow

Earnings from operations of \$20.5 million (\$1.42 per share) were 32% higher than \$15.5 million (\$1.08 per share) in 1976. Cash flow from operations increased 23% to \$42.8 million (\$2.97 per share) from \$34.7 million (\$2.41 per share) in 1976.

Return from operations on shareholders' equity reached 18.6% compared with 12.0% in 1976. Return on total capital employed (earnings from operations, divided by total assets less current liabilities) rose to 14.9% from 9.9% in 1976.



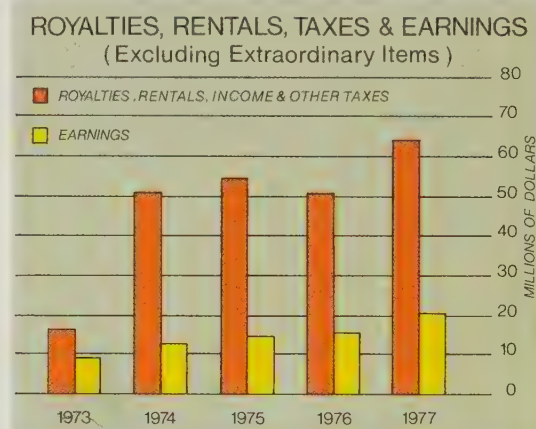
A dividend of \$0.26 per share was paid on April 15, 1977. That amount was in compliance with the Anti-Inflation Act which limited payment to 25% of the Company's net earnings in 1975. The payment amounted to 18% of 1977 net earnings.

Financial results for each quarter were:

	Revenues	Cash Flow	Net Earnings
First quarter	\$20,120,000	\$10,358,000	\$ 5,593,000
Second quarter	18,455,000	9,334,000	4,806,000
Third quarter	20,179,000	9,982,000	5,245,000
Fourth quarter	23,644,000	13,111,000	4,845,000
Total	\$82,398,000	\$42,785,000	\$20,489,000

The accompanying graph sets out a comparison of the Company's earnings with total payments to governments in the form of royalties, rentals, income taxes and other direct taxes on the Company's opera-

tions. Additional payments made to governments, not incorporated in the graph, include land bonuses and sales taxes.

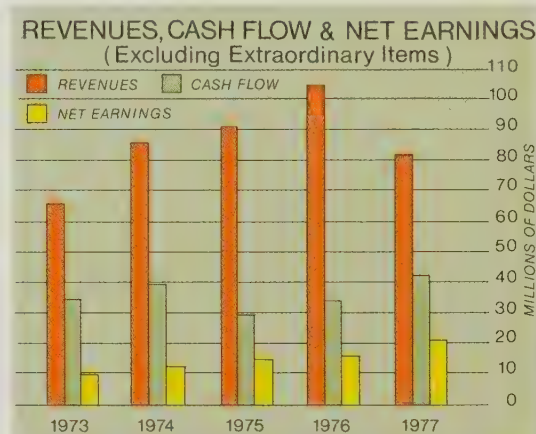


Revenues

For comparative purposes 1976 refining and marketing revenues are omitted in the following discussion.

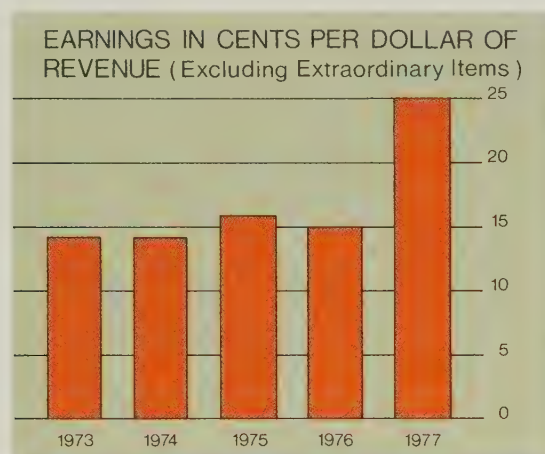
Revenues increased in 1977 by 23% to \$82.4 million. Production revenues were up 27% to \$80.2 million while other revenue was down 43% to \$2.2 million. The decrease in other revenue was caused by reduced interest income due to a lower level of surplus funds available for investment. The table on the next page shows the source of revenues with comparable data for 1976.

The following bar graph illustrates revenues, cash flow and net earnings from all operations, including refining and marketing, for the past five years.



Higher production revenue in 1977 was due almost entirely to price increases which occurred during

1976 and further increases in 1977. Union's average 1977 selling price for crude oil and natural gas liquids was \$9.73 per barrel, for natural gas \$1.03 per



	1977	1976	Increase (Decrease) Percent
Crude oil and natural gas liquids			
Alberta	\$38,535,000	\$34,324,000	12
British Columbia .	4,771,000	4,624,000	3
Saskatchewan-Manitoba	15,177,000	10,121,000	50
	<u>58,483,000</u>	<u>49,069,000</u>	19
Natural Gas			
Alberta	13,350,000	10,840,000	23
British Columbia .	7,203,000	2,595,000	178
Saskatchewan-Manitoba	290,000	140,000	107
	<u>20,843,000</u>	<u>13,575,000</u>	54
Sulphur			
Alberta	874,000	550,000	59
Total production revenue	80,200,000	63,194,000	27
Interest and other income	2,198,000	3,828,000	(43)
Total	<u>\$82,398,000</u>	<u>\$67,022,000</u>	23
Production revenue by province			
Alberta	\$52,759,000	\$45,714,000	15
British Columbia .	11,974,000	7,219,000	66
Saskatchewan-Manitoba	15,467,000	10,261,000	51
Total	<u>\$80,200,000</u>	<u>\$63,194,000</u>	27

thousand cubic feet, and for sulphur \$12.43 per long ton.

The accompanying table indicates the increasing significance of natural gas revenue which rose 54% in 1977 and now accounts for 26% of production revenue as compared to 21% in 1976.

Details of changes in production volumes are provided in the production section of this report.

Expenses

For comparative purposes 1976 refining and marketing expenses are omitted in the following discussion.

Total expenses, not including income taxes, were \$43.1 million, 3% higher than \$42.0 million in 1976.

Exploration expenses, including mineral operations and rentals on unproven lands, were \$5.8 million, up 11%. Provisions for land and dry hole write-offs were up 5% to \$14.6 million. The increases in these expenses are attributed to the significant expansion of the Company's exploration activity.

Production expenses were up 16% to \$13.7 million as a result of new production, increased demand for Saskatchewan medium crude oil and inflationary cost increases.

Charges for depreciation were reduced by 24% to \$4.0 million and administrative and general expense was down 12% to \$4.2 million. These reductions are mainly attributable to disposition of refining and marketing assets in 1976.

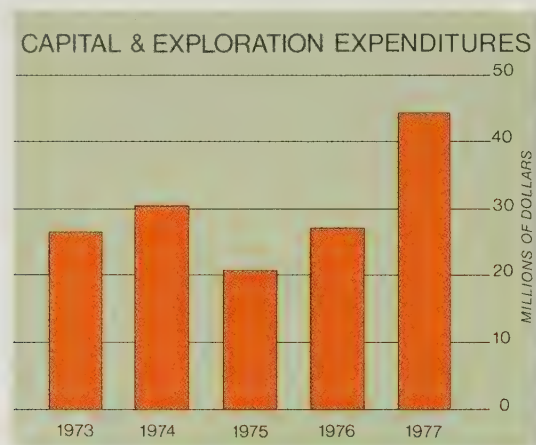
Income Taxes

Provisions for current and deferred taxes totalled \$18.8 million, a 62% increase over \$11.6 million in 1976. The Company's effective rate of tax on pre-tax earnings rose to 48% from 43% in 1976. These increases resulted from higher production revenues and the higher royalties which are treated, for income tax purposes, as income in the hands of producers. Federal and provincial rebates and allowances do not fully offset the treatment of royalty payments as income.

Capital and Exploration Expenditures

Capital and exploration expenditures totalled \$44.1 million as compared to \$27.0 million in 1976. Details of these expenditures are provided in the Financial and Operating Summary on page 24. Petroleum exploration expenditures accounted for approximately 75% of total 1977 spending. As a result of exploration success, outlays for facilities and development drilling

should increase to a larger percentage of total spending in future years. Although expenditures for mineral exploration and development were a small percent-



tage of the total, they were up 174% to \$2.0 million in 1977 and should increase slightly in 1978.

In 1977, 81% of total capital and exploration expenditures were in Alberta, 14% in British Columbia and 3% in Saskatchewan. The remaining 2% was spent in other areas of Canada and Bangladesh.

Working Capital

Cash flow was more than sufficient to provide for the significantly higher level of expenditures and the dividend paid to shareholders in 1977. At year end working capital was \$26.6 million, which included \$17.9 million in cash and short term investments.

Summary and Outlook

Record levels of earnings, cash flow and capital spending were achieved in 1977 and the Company expects further improvement in 1978. Current working capital and anticipated cash flow will provide for the increased expenditures planned for 1978.

Accounting Changes

It is considered appropriate to comment on a number of possible changes in accounting practices in Canada and the United States which could have an impact on financial reporting by Canadian resource companies.

Reporting of financial data on a basis that would reflect the influence of inflation on profits has received a great deal of public comment for some time. There is no doubt that replacement costs of corporate assets would be higher than those values recorded in the accounts on the basis of historical costs. Providing

for depreciation, depletion and amortization on a current replacement costs basis would result in reduced earnings. Accounting and regulatory bodies in both Canada and the United States are continuing their discussions on possible changes in reporting procedures. At present there is not general resource industry agreement on the merits of, or best method for, reporting the impact of inflation on financial results. The Company believes that providing current value financial data would serve no useful purpose until generally accepted guidelines are established.

Another issue which could affect the Company's financial reporting is the recent Financial Accounting Standards Board release in the United States that recommends the adoption of the "successful efforts" basis of reporting for oil and gas operations. If such reporting becomes a regulatory requirement in the United States it could affect reporting within the oil and gas industry in Canada. The Company has been using a form of successful efforts reporting but the specific proposals in the United States, if generally adopted in Canada, could require some changes in the methods the Company uses to charge its exploration and development costs against earnings. This is a relatively new development and a detailed evaluation has not been completed. It is believed, however, that such changes would not materially affect the Company's current earnings.

Another recent development which could influence financial reporting by the oil and gas industry in Canada, relates to studies still underway in the United States. The studies are the result of suggestions that oil and gas companies should include, with their financial reporting, estimates of future earnings and the present value of reserves. At the present time no guidelines have been adopted and there does not appear to be any move towards this type of reporting in Canada.

The Company will continue to review all proposed reporting practices in Canada and will adopt changes when it appears that such changes would provide meaningful comparative information.

UNION OIL COMPANY OF CANADA LIMITED
and its wholly owned subsidiary

Consolidated Statement of Earnings

Year ended December 31

	1977	1976
Revenues		
Sales of crude oil, natural gas, natural gas liquids and sulphur	\$80,200,000	\$ 63,194,000
Sales of refined products	—	36,880,000
Interest and other income	2,198,000	4,521,000
Total revenues	<u>82,398,000</u>	<u>104,595,000</u>
Expenses		
Production	13,706,000	11,799,000
Exploration — petroleum	3,923,000	3,439,000
— minerals	190,000	375,000
Rentals on unproven lands	1,647,000	1,392,000
Amortization of unproven lands	10,588,000	10,919,000
Depletion	883,000	1,114,000
Depreciation	3,950,000	5,211,000
Dry holes and abandonments	4,015,000	3,034,000
Refining and marketing	—	35,513,000
General and administrative	4,171,000	4,713,000
Total expenses	<u>43,073,000</u>	<u>77,509,000</u>
Earnings from operations before income taxes	39,325,000	27,086,000
Income taxes — current (Note 4)	15,976,000	12,660,000
— deferred (Note 4)	2,860,000	(1,060,000)
Earnings from operations before extraordinary gain	20,489,000	15,486,000
(per share — 1977 \$1.42; 1976 \$1.08)		
Sale of assets (after income taxes; current \$4,690,000, deferred (\$1,210,000)) (Note 1)	—	7,227,000
Net Earnings		
(per share — 1977 \$1.42; 1976 \$1.58)	<u>\$20,489,000</u>	<u>\$ 22,713,000</u>

Consolidated Statement of Retained Earnings

Year ended December 31

	1977	1976
Balance at beginning of year	\$ 96,960,000	\$77,271,000
Net earnings for the year	20,489,000	22,713,000
	<u>117,449,000</u>	<u>99,984,000</u>
Dividend paid	3,744,000	3,024,000
Balance at end of year	<u>\$113,705,000</u>	<u>\$96,960,000</u>

See Summary of Accounting Policies and Notes to the Financial Statements.

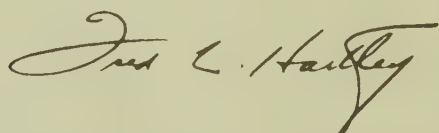
UNION OIL COMPANY OF CANADA LIMITED
and its wholly owned subsidiary

Consolidated Balance Sheet

December 31

	1977	1976
Assets		
Current Assets		
Cash	\$ 411,000	\$ 509,000
Short term deposits	17,525,000	13,776,000
Accounts receivable (Note 1)	17,500,000	20,561,000
Inventories		
Sulphur	218,000	218,000
Materials and supplies	3,120,000	3,120,000
Prepaid expenses	1,136,000	1,086,000
	<u>39,910,000</u>	<u>39,270,000</u>
Property, Plant and Equipment, at cost (Notes 1, 2 and 3)	210,154,000	189,509,000
Less: Accumulated depreciation, depletion and amortization	91,941,000	86,327,000
	<u>118,213,000</u>	<u>103,182,000</u>
Other Assets		
Long term receivables	732,000	959,000
Investment in non-controlled companies, at cost	1,012,000	1,012,000
Operating and performance deposits	1,046,000	879,000
	<u>2,790,000</u>	<u>2,850,000</u>
	<u>\$160,913,000</u>	<u>\$145,302,000</u>

Approved by the Board of Directors



Director



Director

See Summary of Accounting Policies and Notes to the Financial Statements

	1977	1976
Liabilities		
Current Liabilities		
Accounts payable and accrued liabilities	\$ 13,279,000	\$ 12,237,000
Income taxes payable	—	5,050,000
	<u>13,279,000</u>	<u>17,287,000</u>
Deferred Income Taxes (Note 4)	28,955,000	26,095,000
	<u>42,234,000</u>	<u>43,382,000</u>
Shareholders' Equity		
Share Capital (Note 5)		
Authorized		
22,500,000 shares without par value		
Issued and fully paid		
1977 — 14,400,990 shares	4,974,000	
1976 — 14,399,190 shares		4,960,000
	<u>4,974,000</u>	<u>4,960,000</u>
Retained Earnings	113,705,000	96,960,000
	<u>118,679,000</u>	<u>101,920,000</u>
	<u>\$160,913,000</u>	<u>\$145,302,000</u>

UNION OIL COMPANY OF CANADA LIMITED
and its wholly owned subsidiary

Consolidated Statement of Changes in Financial Position

Year ended December 31

	1977	1976
Source of Funds		
Total production revenue	\$ 82,398,000	\$ 67,022,000
Less expenditures involving the outlay of funds	39,613,000	34,379,000
Funds provided from exploration and production operations	42,785,000	32,643,000
Funds provided from refining and marketing operations	—	2,061,000
Disposal of property, plant and equipment	113,000	326,000
Issue of shares (Note 5)	14,000	—
Net decrease in other assets	60,000	652,000
Disposal of refining and marketing assets (after current income taxes of \$4,690,000)	—	27,370,000
	<u>42,972,000</u>	<u>63,052,000</u>
Use of Funds		
Capital expenditures	38,341,000	21,824,000
Less provincial incentives (Note 3)	(3,761,000)	(3,385,000)
Dividend paid	3,744,000	3,024,000
Reduction of capital	—	73,318,000
	<u>38,324,000</u>	<u>94,781,000</u>
Increase (decrease) in working capital	4,648,000	(31,729,000)
Working capital at beginning of year	21,983,000	53,712,000
Working capital at end of year	<u>\$ 26,631,000</u>	<u>\$ 21,983,000</u>
Consisting of:		
Current assets	\$ 39,910,000	\$ 39,270,000
Less current liabilities	13,279,000	17,287,000
	<u>\$ 26,631,000</u>	<u>\$ 21,983,000</u>

See Summary of Accounting Policies and Notes to the Financial Statements.

Auditors' Report

To the Shareholders of Union Oil Company of Canada Limited

We have examined the consolidated balance sheet of Union Oil Company of Canada Limited and its wholly owned subsidiary as at December 31, 1977, and the consolidated statement of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1977 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Coopers & Lybrand

Calgary, February 3, 1978

Chartered Accountants

Summary of Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of Union Oil Company of Canada Limited and its wholly owned subsidiary Union Oil Holdings Limited.

Inventories

Valuation of inventories is at or below average cost but does not exceed net realizable value.

Leasehold Costs

The cost of acquisition of oil and gas rights, which includes a portion of the costs of wells drilled to earn an interest in such rights and the cost of geophysical surveys which result in acquisition or retention of those rights, are capitalized. Such costs related to unproven oil and gas rights are amortized over the estimated period of retention of those rights and when such rights are surrendered their original cost is charged against the accumulated amortization. When unproven lands become productive the original costs are transferred to proven and, like the acquisition costs of producing properties, are charged against earnings by an annual provision for depletion calculated on a unit of production basis. Total proven reserves, both developed and undeveloped, are used in this calculation.

All oil sands and heavy oil expenditures, other than for wells drilled to delineate the extent of deposits, which are treated as exploration and development costs, are capitalized as costs of oil and gas rights and are amortized over the estimated period of retention of those rights.

The cost of acquisition of coal and mineral rights, including a portion of the costs of field exploration work carried out to earn such rights or which result in the acquisition of such rights, are capitalized. Such costs are amortized over the estimated period of retention of those rights.

Exploration and Development Costs

The costs of drilling exploratory wells are charged to expense as incurred, except that a portion of the costs of those wells which are drilled to earn interests in petroleum and natural gas rights are capitalized. The costs of successful wells are capitalized. The costs of geophysical surveys in which the Company is an initial participant and the costs of coal and mineral field exploration programs are capitalized and such costs which do not result in the acquisition or retention of lands are subsequently charged to expense when the results are evaluated. The costs of geophysical or geological data purchased from contractors or other operators are expensed as incurred.

Depletion and Depreciation

The costs of drilling successful wells and costs of production equipment and facilities, including gas processing plants, are capitalized and subsequently charged to expense as depletion and depreciation which are calculated on the unit of production basis using in the calculation only proven developed reserves.

Costs of general facilities are depreciated on the straight line basis over the estimated useful life of the facility.

Income Taxes

The Company follows the tax allocation method of accounting for deferred income taxes which arise as a result of recording depletion, depreciation and amortization for accounting purposes at rates other than those allowed for income tax purposes.

Notes to the Financial Statements

Note 1 — Sale of Assets

By agreement dated April 23, 1976, the Company, subject to approval by the Foreign Investment Review Agency, sold all of its refining and marketing assets to Husky Oil Operations Ltd. Following receipt of approval from the Foreign Investment Review Agency, the effective date of sale was November 1, 1976. Comparative figures for 1976 in the financial statements include the results of the operations of the refining and marketing divisions for the ten months ended October 31. Accounts receivable at December 31, 1976 included amounts of \$1,100,000 applicable to those operations and an amount of \$5,200,000 due from Husky on the sale of the inventories. All of those amounts were paid early in 1977.

Note 2 — Property, Plant and Equipment

December 31, 1977

	Gross Investment at Cost	Accumulated Depreciation, Depletion and Amortization	Net Investment	Net Investment December 31, 1976
Unproven lands — petroleum	\$ 59,629,000	\$16,954,000	\$ 42,675,000	\$ 32,707,000
— mineral	1,089,000	96,000	993,000	482,000
Proven lands	42,146,000	25,462,000	16,684,000	15,643,000
Work in progress — petroleum	395,000	—	395,000	440,000
— mineral	1,599,000	—	1,599,000	1,251,000
Oil and gas wells and facilities	82,582,000	37,179,000	45,403,000	41,786,000
Gas plants and facilities	19,487,000	10,766,000	8,721,000	9,484,000
Other facilities and equipment	3,227,000	1,484,000	1,743,000	1,389,000
TOTAL	\$210,154,000	\$91,941,000	\$118,213,000	\$103,182,000

Note 3 — Government Incentives

Following enactment in 1974 of federal income tax legislation which assessed income taxes against the resource industries on amounts paid to governments as royalties and other levies, each of the three western provinces initiated incentive programs to encourage exploration and development within their borders. Amounts received during 1977 under the programs totalled \$3,805,000 (\$3,590,000 in 1976). Of that total, \$44,000 (\$205,000 in 1976) was credited directly to operating costs, \$1,750,000 (\$1,565,000 in 1976) was initially credited to capital accounts and subsequently written off during the year and \$2,011,000 (\$1,820,000 in 1976) remained credited to capital accounts at the year end. A further amount of \$28,000 (\$400,000 in 1976) was applied for under the federal Industrial Research and Development Incentives Act and was credited directly to other income.

Note 4 — Income Taxes

In calculating taxable income, the Company is permitted to deduct exploration and development expenses and to provide for capital cost allowances at rates which vary from the corresponding write-offs and depreciation recorded in the accounts. Any excess of such costs not used in one year may be carried forward to be deducted in calculating future taxable income. At December 31, 1977, exploration and development expenses totalling approximately \$22,300,000 were carried forward. At the same date, approximately \$5,700,000 of unclaimed capital costs remained. The comparable figures at December 31, 1976 were approximately \$13,900,000 and \$6,900,000.

In accordance with the income tax allocation basis of accounting, the company has provided in the accounts for income taxes deferred by reason of all timing differences in claiming costs for tax purposes and charging these costs against earnings for financial accounting purposes. In 1977, costs deducted from income for purposes of calculating income taxes exceeded those charged against earnings in the accounts with the result that income taxes were deferred to the extent of \$2,860,000. In 1976, costs charged against income in the accounts exceeded those claimed for tax purposes resulting in a reduction in deferred income taxes of \$2,270,000.

The Income Tax Acts provide that certain expenditures may be carried forward for use in calculating depletion to be applied in determining taxable income. At December 31, 1977, the amount of those expenditures which had not been applied, only 33¹/₃% of which may constitute earned depletion, was approximately \$24,600,000 (\$24,100,000 at December 31, 1976).

Note 5 — Share Capital

During the year, a stock option to purchase 5,400 no par value shares of the Company was granted to an employee at an option price of \$10.35. Options to purchase 6,800 shares which were granted March 8, 1974 at an option price of \$11.95 per share, expired.

During 1977, 1,800 no par value shares were issued for cash pursuant to stock options granted in 1976. The total consideration of \$13,968 was credited to share capital.

At December 31, 1977, options to purchase no par value shares of the Company were outstanding as follows:

Date of Grant	Held By		Option Price
	Officers (one of whom is a director)	Employees	
September 17, 1970	—	3,100	\$10.65
March 8, 1974	—	4,350	11.95
December 6, 1976	89,330	29,615	7.76
September 23, 1977	—	5,400	10.35
TOTAL	<u>89,330</u>	<u>42,465</u>	

Option prices are 90% of the market price at the date of grant. In the case of the 1970 options, effect has been given to the three for one share split which occurred in November, 1972.

Note 6 — Remuneration of Directors and Officers

During the year there were six directors and nine officers, two of whom served also as directors. During 1977, aggregate direct remuneration payable by the Company and its consolidated subsidiary to the directors and senior officers of the Company amounted to \$439,146, of which \$3,500 was paid as directors' fees.

During the year a loan of \$120,000 was made to an officer to assist him with the purchase of a personal residence.

Note 7 — Commitments and Contingencies

In accordance with relevant regulations, the Company has issued non-interest bearing demand notes which are on deposit with the governments of Canada, Alberta and Manitoba to guarantee the performance of exploratory work in respect of certain Crown oil and gas rights granted to the Company. These demand notes totalled \$291,000 at December 31, 1977.

The Company is contingently liable for the payment of principal (to a maximum of \$2,160,000 at December 31, 1977) and interest in respect to certain debentures of a pipeline company of which Union Oil Company of Canada Limited is a shareholder.

Note 8 — Anti-Inflation Act

The Company's results for 1978 will not be directly affected by the anti-inflation guidelines regarding prices and profits because controls over production revenues are governed by different legislation. The amount of dividends which the Company may declare prior to October 13, 1978 will, however, be restricted by the current anti-inflation legislation.

Note 9 — Employees' Retirement Plan

The Company has a retirement plan covering essentially all employees. As of January 1, 1977, the most recent actuarial review date, the estimated plan liabilities exceeded plan assets by approximately \$740,000. This under-funding resulted from changes made to the provisions of the plan from time to time and is being funded over a maximum period of fifteen years as required by applicable legislation.

Note 10 — Comparative Figures

Certain 1976 figures provided for purposes of comparison have been restated to conform to the presentation used in the current year. These changes have no effect on the 1976 earnings.

Financial and Operating Summary

Financial

(in thousands of dollars, except where otherwise specified)

	1977	1976	1975	1974	1973
Income from all sources	\$ 82,398	\$ 104,595	\$ 91,727	\$ 85,518	\$ 65,259
Cash expenses (including current income taxes)	39,613	69,891	62,438	46,359	30,890
Cash flow from operations	42,785	34,704	29,289	39,159	34,369
Dollars per share	2.97	2.41	2.03	2.72	2.39
Non-cash expense	19,436	20,278	16,847	20,407	21,005
Provision for deferred income taxes	2,860	(1,060)	(1,921)	6,500	4,227
Earnings from operations	20,489	15,486	14,363	12,252	9,137
Dollars per share	1.42	1.08	1.00	0.85	0.63
Non-recurring profit on sale of assets	—	7,227	1,048	—	—
Dollars per share	—	0.50	0.07	—	—
Working capital	26,631	21,983	53,712	48,852	34,499
Property, plant and equipment, net	118,213	103,182	126,700	127,540	122,004
Investments and other assets	2,790	2,850	3,502	2,450	3,547
Total assets employed	147,634	128,015	183,914	178,842	160,050
Accumulated provision for deferred income taxes	28,955	26,095	28,365	30,065	23,565
Shareholders' equity	118,679	101,920	155,549	148,777	136,485
Dollars per share	\$ 8.24	\$ 7.08	\$ 10.80	\$ 10.33	\$ 9.48
Return from operations on average shareholders' equity (percent)	18.6	12.0	9.4	8.6	6.9
Number of shares issued and outstanding	14,400,990	14,399,190	14,399,190	14,399,190	14,395,440
Number of shareholders	1,292	1,053	992	983	915
Dividend paid	\$ 3,744	\$ 3,024	\$ 8,639	\$ —	\$ —
Dollars per share	0.26	0.21	0.60	—	—
Market price of shares — high	16.87	13.25	9.50	14.00	21.25
— low	\$ 8.75	\$ 7.12	\$ 7.00	\$ 6.75	\$ 12.50
Capital and exploration expenditures					
Development drilling	\$ 4,792	\$ 3,614	\$ 3,368	\$ 1,517	\$ 4,177
Oil, gas and gas plant facilities	1,689	1,961	3,168	2,861	2,021
Exploratory drilling	9,225	6,842	1,267	9,971	13,552
Geophysical surveys	3,892	2,263	2,700	3,737	1,088
Mineral exploration	1,471	668	620	529	232
Acquisition of oil and gas properties	14,025	6,242	1,962	5,455	1,110
Acquisition of mineral properties	533	63	22	—	—
Heavy oil research	2,342	12	3,396	809	170
Refining and marketing	—	126	754	1,937	1,105
Other	372	33	15	290	85
Total capital expenditures	38,341	21,824	17,272	27,106	23,540
Exploration expenses (including rentals)	5,760	5,206	3,467	3,033	2,827
Total	\$ 44,101	\$ 27,030	\$ 20,739	\$ 30,139	\$ 26,367

Operating

Average gross daily production					
Crude oil and natural gas liquids (bbls.)	27,974	27,399	30,119	39,097	43,042
Natural gas (mcf)	69,016	68,461	66,742	80,809	72,853
Sulphur (long tons)	198	228	270	308	308
Gross proven reserves					
Crude oil and natural gas liquids (thousands of bbls.)	117,578	126,727	137,031	128,157	147,739
Natural gas (mmcf)	632,582	595,692	622,833	626,586	640,795
Sulphur (thousands of long tons)	885	1,000	1,205	979	1,192
Petroleum land holdings (thousands of net acres)	6,069	6,494	6,423	8,430	6,221
Mineral land holdings (thousands of net acres)	255	308	262	1,041	995
Number of employees	303	272	337	360	352

Directors

at February 24, 1978

C. S. Brinegar

*Senior Vice President
Union Oil Company of California
Los Angeles, California*

R. A. Burke

*Senior Vice President
Union Oil Company of California
Los Angeles, California*

C. W. Dumett, Jr.

*President
Union Oil Company of Canada Limited
Calgary, Alberta*

Fred L. Hartley

*Chairman and President
Union Oil Company of California
Los Angeles, California*

C. F. Parker

*Senior Vice President
Union Oil Company of California
Los Angeles, California*

J. M. Tory, Q.C.

*Barrister & Solicitor
Tory, Tory, DesLauriers & Binnington
Toronto, Ontario*

Head office

335 Eighth Avenue S.W.,
Calgary, Alberta

Transfer Agent and Registrar

The Royal Trust Company,
Calgary, Montreal, Toronto,
Winnipeg, Vancouver

Subsidiary

Union Oil Holdings Limited

Stock Exchange Listings

The shares of the Company are listed on
The Toronto, Montreal, Vancouver and
Alberta Stock Exchanges

Auditors

Coopers & Lybrand

Incorporated under the Laws of Canada

Officers and Senior Management

at February 24, 1978

Fred L. Hartley

Chairman of the Board

C. W. Dumett, Jr.

President

E. J. Connor

Vice President, Production

D. B. Jarrett

Vice President, Administration

E. D. B. Laudeman

Vice President, Exploration

J. L. MacLagan

Vice President, Finance, Treasurer

R. G. Byers

General Counsel, Secretary

J. J. Bohnet

Comptroller, Assistant Secretary

D. B. Leitch

General Manager, Minerals



UNION OIL COMPANY OF CANADA LIMITED

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